SECURITIES AND EXCHANGE COMMISSION

17 CFR Part 250

[Release No. 35–26312, File No. S7–11–95]

RIN 3235–AG45

Exemption of Issuance and Sale of Securities By Public-Utility and Nonutility Subsidiary Companies of Registered Public-Utility Holding Companies

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rules.

SUMMARY: The Commission, which today amended rules 45 and 52 under the Public Utility Holding Company Act of 1935 (''Act''), is requesting comment on further amendments. The proposed amendment to rule 52 would permit a subsidiary company of a registered company to issue and sell any security without the need to apply for, or receive, prior Commission approval, where the conditions of the rule are met. The Commission is proposing a conforming amendment to rule 45 with respect to the guaranty of securities. These amendments are intended to eliminate unnecessary regulatory burdens and paperwork associated with seeking Commission approval for routine financings by companies in a registered holding company system.

DATES: Comments must be submitted on or before September 26, 1995.

ADDRESSES: Comments should be submitted in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W., Mail Stop 6–9, Washington, D.C. 20549. Comment letters should refer to File No. S7–11–95. All comment letters received will be available for public inspection and copying in the Commission's Public Reference Room, 450 Fifth Street, N.W., Washington, D.C. 20549.

FOR FURTHER INFORMATION CONTACT: William C. Weeden, Associate Director, Joanne C. Rutkowski, Assistant Director, or Bonnie Wilkinson, Staff Attorney, all at (202) 942–0545, Office of Public Utility Regulation, Division of Investment Management, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549.

SUPPLEMENTARY INFORMATION: The Commission is requesting comment on proposed amendments to rules 45 and 52 (17 CFR 250.45 and 250.52) under the Public Utility Holding Company Act of 1935 [15 U.S.C. 79 et seq.]. Rule 52 has exempted from the requirement of prior Commission approval under section 6(a) the issuance and sale of certain specified types of securities by any subsidiary company of a registered holding company, in accordance with the terms and conditions of the rule. The proposed amendment to rule 52 would broaden the scope of the rule to exempt all types of securities issued and sold by such subsidiary companies, subject to satisfying the other conditions of the rule. A conforming change to rule 45 is also being proposed to conditionally exempt from the requirement of prior Commission approval under section 12(b) any guaranty by a subsidiary company of debt securities issued by any other subsidiary company.

The Commission is also proposing to rescind the statements of policy with respect to first mortgage bonds and preferred stock (''Statements of Policy'') and seeks comment on this proposal.[1]

Introduction

Rule 52 exempts from the requirement of prior Commission authorization under section 6(a) the issue and sale of certain specified types of securities by both public-utility and nonutility subsidiary companies of registered public-utility holding companies.[2] Rule 52 also exempts from the requirement of prior Commission authorization under section 9(a)(1) the acquisition by a company in a registered holding company system of any securities issued by any associate company pursuant to the rule.[3]

Rule 52, as originally adopted in 1990, was limited to specified types of securities issued by public-utility companies. The rule was amended in 1992 to, among other things, expand the types of securities within the exemption;[4] and the Commission has today further amended the rule in order to expand the categories of securities covered, to make the exemption more useful in connection with other common forms of intrasystem financing, and to extend the exemption to nonutility companies. As so amended, the rule provides a conditional exemption from the requirement of prior Commission approval for the issue and sale by both public-utility and nonutility subsidiary companies of a registered holding company of any common stock, preferred stock, bond, note or other form of indebtedness of which it is the issuer (excluding guaranties), provided that, in the case of any note issued to an associate company, the interest rate and maturity date of such note are designed to parallel the effective cost of capital of that associate company. To qualify for exemption under rule 52, the issue and sale must be solely for the purpose of financing the business of the subsidiary company and, if the subsidiary company is a public-utility company, must be expressly authorized by the relevant state commission.

The Commission is today proposing a further amendment to rule 52 to exempt the issue and sale of any security by a subsidiary company in a registered holding company where the conditions of the rule are otherwise met. This additional change is intended to eliminate unneeded regulation of routine financings by existing subsidiaries of a registered holding company. The Commission is also proposing a further change to rule 45 to conform the exemption from section 12(b), which is provided by rule 45, to the exemption from section 6(a), which is provided by rule 52. Such a conforming amendment is necessary because a guaranty may be both a security under section 6(a) and an extension of credit under section 12(b).

The Commission is also proposing to rescind the Statements of Policy.

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[1] Holding Co. Act Release Nos. 13105 and 13106 (Feb. 16, 1956), as amended in Holding Co. Act Release Nos. 16369 (May 8, 1969) and 16758 (June 22, 1970).

[2] Section 6(a) requires Commission approval under the standards of section 7 of the issue and sale of any security of a registered holding company or its subsidiary company.

Section 6(b) authorizes the Commission to exempt from the declaration requirements of section 6(a):

> the issue or sale of any security by any subsidiary company of a registered holding company, if the issue and sale of such security are solely for the purpose of financing the business of such subsidiary company and have been expressly authorized by the State commission of the State in which such subsidiary company is organized and doing business. * * *

In section 6(a), the Congress intended ''to exempt the issue of securities by subsidiary companies in cases where holding company abuses are unlikely to exist.'' H.R. Conf. Rep. No. 1903, 74th Cong., 1st Sess. 66–67 (1935). See generally Holding Co. Act Release No. 25058 (Mar. 9, 1990), 55 FR 11362 (Mar. 28, 1990) (adopting rule 52), and Holding Co. Act Release No. 25573 (July 7, 1992), 57 FR 31120 (July 14, 1992) (amending rule 52).

[3] Section 9(a)(1) requires prior Commission approval under the standards of section 10 for the acquisition of securities by a registered holding company or its subsidiary company. Section 9(c)(3) provides a limited exception from this requirement for the acquisition of:

> such commercial paper and other securities, within such limitations, as the Commission may by rules and regulations or order prescribe as appropriate in the ordinary course of business of a registered holding company or subsidiary company thereof and as not detrimental to the public interest or the interest of investors or consumers.

The exemption under rule 52 does not apply to the issuance and acquisition of securities to form a new subsidiary company of a registered holding company.

[4] See fn. 2, *supra.*

Discussion

In the 1992 release inviting comments on the proposed amendment to rule 52, adopted today, the Commission requested comments on whether the exemption under rule 52 should also be extended to exempt financing transactions involving other securities, in particular guaranties of debt securities issued by other subsidiary companies.

All of the registered holding companies commenting on the proposed amendment [5] favored extending the exemption to other types of securities, including guaranties. Guaranties by parent companies are frequently used in conjunction with borrowings by their subsidiary companies, and have been approved by order in countless instances.[6] Depending on materiality, such guaranties are required to be disclosed in financial statements. Further, as several commenters noted,[7] guaranties of affiliate company obligations by public-utility companies are subject to public utility commission approval in many states.

Several commenters [8] also supported expansion of rule 52 to exempt other categories of securities, particularly in the context of nonutility subsidiary financings. One holding company,[9] for example, noted the widespread use of partnership interests and other types of securities in nonutility financing, particularly in the context of project finance, and recommended the inclusion of such securities in rule 52(b).[10] The Commission is aware that a majority of states now have adopted limited liability company statutes which create a hybrid between partnerships and corporations.[11] This is an increasingly popular form of business enterprise. Based upon the Commission's experience in recent years with individual applications, it is clear that the kinds and types of securities issued by nonutility subsidiaries, including independent power subsidiaries, tend to vary more than those issued by public-utility subsidiaries.

The Commission is proposing to amend rule 52 to conditionally exempt the issue and sale of all types of securities by public-utility and nonutility subsidiaries alike. Because of the extensive reporting requirements imposed by the Act and other federal securities laws, and the far greater scrutiny of reporting companies since the passage of the Act sixty years ago, the Commission believes that it may be appropriate to condition the exemption under rule 52 solely by reference to the literal requirements of section 6(b), without regard to the form of the security issued.

In this connection, the Commission notes that it has exercised jurisdiction under sections 6(a) and 7 of the Act over interest rate swap agreements and related instruments.[12] Comment is requested on the extent, if any, to which such transactions should be excluded from the rule proposed today.

The Commission is also considering whether compliance with rule 52(b)(2) [13] should be required in situations where a nonutility subsidiary of a registered holding company issues a security that is acquired by another nonutility subsidiary in the same holding company system. Comment is requested on whether rule 52(b)(2) should be amended to create an exception for such situations.

A guaranty of debt securities issued by another subsidiary company is itself a security under the Act,[14] the issuance and sale of which is subject to the declaration requirement of section 6(a), unless exempted under section 6(b). In addition, the guaranty by a subsidiary company of any obligation of another subsidiary company is subject to section 12(b) and rule 45(a) thereunder.[15] An agreement to assume joint liability, as co-maker or otherwise, with respect to the indebtedness of another company is the functional equivalent of a guaranty, and is also subject to both sections 6(a) and 12(b).

Rule 45(a), with exceptions not relevant here, prohibits the issuance of guaranties and similar undertakings by a subsidiary company without the filing of a declaration.[16] We believe, however, that any guaranty or similar undertaking with respect to the indebtedness of another subsidiary company that is issued pursuant to the exemption provided by rule 52 should itself be exempt under rule 45. Accordingly, we are proposing to add a new paragraph to rule 45(b) to conform the related exemptions.[17]

In connection with the amendments to rules 52 and 45 adopted today by the Commission, some commenters have expressed concern that public-utility subsidiaries of registered holding companies and their customers need protection from the financial effects of financing transactions, particularly in the context of nonutility ventures that are not otherwise subject to effective state oversight.[18] The proposed expansion of the exemptions under rules 52 and 45 may heighten these concerns, and the Commission seeks the views of all parties on these issues. As a result, the Commission requests comments as to whether protection is needed and, if so, what form it should take. Commenters are invited to address the need for limitations based on (a) the registered holding company system's capitalization ratios; (b) the financial condition of the registered holding company system; (c) the extent of past losses incurred by registered holding companies in connection with past nonutility ventures; and (d) any other basis specified by the commenter. The

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[5] The registered holding companies submitting comments were American Electric Power Company, Inc. (''AEP''), Allegheny Power System, Inc. (''APS''), Consolidated Natural Gas Company (''CNG''), Central and South West Corporation, Eastern Utilities Associates, General Public Utilities Corporation (''GPU''), and New England Electric System.

[6] See, *e.g.*, Eastern Utilities Assocs., Holding Co. Act Release No. 26266 (April 5, 1995)(guaranty by parent holding company of obligations of nonutility subsidiary); American Electric Power Co., Holding Co. Act Release No. 26267 (April 5, 1995)(same); Jersey Central Power & Light Co., Holding Co. Act Release No. 26246 (March 6, 1995)(guaranty by utility of payment obligations on preferred limited partnership interests of investment subsidiary); and Southern Co., Holding Co. Act Release No. 26221 (Jan. 25, 1995)(guaranty by holding company of debt, lease obligations and installment purchase obligations of nonutility subsidiary).

[7] AEP 3 and GPU at 4.

[8] See generally AEP at 3, APS at 2, and CNG at 3.

[9] GPU at 3.

[10] Many of the nonutility investments approved by the Commission in recent years have involved joint ventures with nonassociate companies. It is almost always desirable for the joint venture partners to invest directly or indirectly in an entity (such as a partnership) which for federal and state income tax purposes is treated as a partnership, rather than as a corporation, so that the income, loss and credits associated with the business can be reported directly by the joint venture partners.

[11] We understand that limited liability companies may be treated for tax purposes as partnerships, rather than taxed as corporations.

[12] These related instruments include products referred to as interest rate caps, floors and collars. Registered holding companies and subsidiaries have been using such instruments to limit the range within which the interest rate on the debt underlying such instrument will vary.

[13] Rule 52(b)(2) requires that the interest rate and maturity date of a debt security issued by a nonutility company to an associate company be designed to parallel the effective cost of capital of the associate company.

[14] See Holding Company Act section 2(a)(16)(definition of security), 15 U.S.C. 79b(a)(16).

[15] Section 12(a) prohibits the guaranty by subsidiary companies of debt issued by a registered holding company. 15 U.S.C. 79*l*(a).

[16] At present, rule 45(b)(6) exempts certain guaranties ''in the ordinary course of business.'' The rule by its terms does not apply to a guaranty of a subsidiary's indebtedness for borrowed money.

[17] Under our proposal, it is possible that a subsidiary company providing a guaranty may be exempt from section 12(b) by reason of the proposed amendment to rule 45, but fail to satisfy the conditions for exemption from section 6(a) provided by rule 52.

[18] *See* the discussion of the comments of the City of New Orleans in the companion release published today in the **Federal Register**.

Commission also seeks comment on whether the rules should incorporate any requirements of notice to interested state commissions of the consummation of financing by nonutility subsidiaries of registered holding companies.

The Commission also proposes to rescind the Statements of Policy. The Statements of Policy were formulated by the Commission's staff nearly forty years ago to specify the terms to be included in new issues of first mortgage bonds and preferred stock. As the securities markets have developed, the Commission has found that the Statements of Policy have become anachronistic and hinder the ability of registered companies to raise capital. As a result, the Commission has permitted more and more deviations on a case-by-case basis from the requirements of the Statements of Policy.[19] In addition, in 1992, for similar reasons, the Commission eliminated compliance with the Statements of Policy as a condition to use of Rule 52.[20] The Commission believes that it is no longer appropriate to require specific terms to be included in securities issues, and requests comment on this proposed rescission.

Conclusion

The Commission believes that the registered holding-company systems should have a greater ability to engage in routine financings without the regulatory burden of prior Commission authorization, and that this may be done without jeopardizing the interests the Act is designed to protect. The rule amendments proposed today are intended to accomplish this purpose.

Regulatory Flexibility Act Certification

Pursuant to Section 605(b) of the Regulatory Flexibility Act, 5 U.S.C. 605(b), the Chairman of the Commission has certified that the proposed amended rules will not, if adopted, have a significant economic impact on a substantial number of small entities. This certification, including the reasons therefor, may be obtained from Bonnie Wilkinson, Office of Public Utility Regulation, Division of Investment Management, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549.

Costs and Benefits

It appears that amended rules 45 and 52 will substantially decrease regulatory compliance costs for the registered holding companies.

Paperwork Reduction Act

The proposed amendment is subject to the Paperwork Reduction Act of 1980 (44 U.S.C. 79 *et seq.*) and will be submitted to the Office of Management and Budget for approval.

Statutory Authority

The Commission is proposing to amend rules 45 and 52 pursuant to sections 6, 9, 12 and 20 of the Act.

List of Subjects in 17 CFR Part 250

Electric utilities, Holding companies, Natural gas, Reporting and recordkeeping requirements, Securities.

Text of Proposed Rules

For the reasons set forth in the preamble, Part 250 of chapter II, title 17, of the Code of Federal Regulations is proposed to be amended as follows:

PART 250—GENERAL RULES AND REGULATIONS, PUBLIC UTILITY HOLDING COMPANY ACT OF 1935

1. The authority citation for part 250 continues to read as follows.

Authority: 15 U.S.C. 79c, 79f(b), 79i(c)(3), 79t, unless otherwise noted.

2. Section 250.45 is amended by adding paragraph (b)(7) to read as follows:

§ 250.45 Loans, extensions of credit, donations and capital contributions to associate companies.

* * * * *

(b) *Exceptions.* * * *

(7) An agreement by any subsidiary company of a registered holding company to assume liability (as guarantor, co-maker, indemnitor, or otherwise) with respect to any security issued by any other subsidiary company in the same holding company system, provided that the issuance and sale of such security is exempt from the declaration requirements of section 6(a) of the Act (15 U.S.C. 79f(a)) pursuant to § 250.52.

3. Section 250.52 is amended by revising paragraphs (a) and (b) to read as follows:

§ 250.52 Exemption of issue and sale of certain securities.

(a) Any registered holding-company subsidiary which is itself a public-utility company shall be exempt from section 6(a) of the Act (15 U.S.C. 79f(a)) and rules thereunder with respect to the issue and sale of any security, of which it is the issuer if:

(1) The issue and sale of such security are solely for the purpose of financing the business of such public-utility subsidiary company;

(2) The issue and sale of such security have been expressly authorized by the state commission of the state in which such subsidiary company is organized and doing business; and

(3) The interest rates and maturity dates of any debt security issued to an associate company are designed to parallel the effective cost of capital of that associate company.

(b) Any subsidiary of a registered holding company which is not a holding company, a public-utility company, an investment company, or a fiscal or financing agency of a holding company, a public-utility company or an investment company shall be exempt from section 6(a) of the Act (15 U.S.C. 79f(a)) and rules thereunder with respect to the issue and sale of any security, of which it is the issuer if:

(1) The issue and sale of such security are solely for the purpose of financing the existing business of such subsidiary company; and

(2) The interest rates and maturity dates of any debt security issued to an associate company are designed to parallel the effective cost of capital of that associate company.

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Dated: June 20, 1995.

By the Commission.

Jonathan G. Katz,

Secretary.

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 95–15837 Filed 6–27–95; 8:45 am]

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SECURITIES AND EXCHANGE COMMISSION

17 CFR Parts 250 and 259

[Release No. 35–26313; File No. S7–12–95]

RIN 3235–AG46

Exemption of Acquisition By Registered Public-Utility Holding Companies of Securities of Nonutility Companies Engaged in Certain Energy-Related and Gas-Related Businesses; Exemption of Capital Contributions and Advances to Such Companies

AGENCY: Securities and Exchange Commission.

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[19] See, e.g., Georgia Power Co., Holding Co. Act Release No. 25033 (Feb. 7, 1990)(authorizing deviation from redemption provisions required by Statement of Policy for first mortgage bonds), and System Energy Resources, Inc., Holding Co. Act Release No. 24318 (Feb. 18, 1987) (authorizing charter amendment with earnings coverage requirement different from Statement of Policy for preferred stock). The Statements of Policy themselves contemplate that ''deviations from these standards should be permitted in appropriate cases.'' Holding Co. Act Release Nos. 13105 and 13106 (Feb. 16, 1956).

[20] Holding Co. Act Release No. 25573 (July 7, 1992), 57 FR 31120 (July 14, 1992).